

No. 12,055

IN THE

United States Court of Appeals  
For the Ninth Circuit

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JAMES G. SMYTH, Collector of Internal  
Revenue of the First Internal Revenue  
Collection District of California,  
*Appellant,*

vs.

CALIFORNIA STATE AUTOMOBILE ASSO-  
CIATION, a corporation,  
*Appellee.*

On Appeal from the United States District Court for the  
Northern District of California.

BRIEF FOR APPELLANT.

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**OPINION BELOW.**

The opinion of the District Court (R. 67-78) is reported in 77 F. Supp. 131.

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**JURISDICTION.**

This appeal involves Federal income and excess profits taxes for the calendar years 1943 and 1944. (R. 4.) The taxes in dispute are in the amount of \$232,865.12 and were paid on September 15, 1945. (R. 81.) Claims for refund were filed on October 23,

1945. (R. 81.) More than six months after the filing of the claims and within the time provided in Section 3772 of the Internal Revenue Code or on May 26, 1948, the taxpayer brought an action in the District Court for recovery of the taxes paid. (R. 2-63.) Jurisdiction was conferred on the District Court by 28 U.S.C., Section 1340. The judgment was entered on March 24, 1948. (R. 90-91.) Within sixty days and on May 20, 1948, a notice of appeal was filed (R. 91-92) pursuant to the provisions of 28 U.S.C., Section 1291.

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### QUESTION PRESENTED.

Was taxpayer, during the taxable years 1943 and 1944, a club, organized and operated exclusively for pleasure, recreation and other nonprofitable purposes within the meaning of Section 101 (9) of the Internal Revenue Code?

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### STATUTE INVOLVED.

Internal Revenue Code:

Sec. 101. EXEMPTIONS FROM TAX ON CORPORATIONS.

The following organizations shall be exempt from taxation under this chapter—

\* \* \* \* \*

(9) Clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes, no part of the net earnings of which inures to the benefit of any private shareholder;

\* \* \* \* \*

[26 U.S.C. 1946 ed., Sec. 101.]

**STATEMENT.**

The District Court found the facts substantially as follows (R. 80-86):

Taxpayer was organized under the laws of California in 1907 as a nonprofit corporation, the purposes of which are substantially as follows (R. 82):

(1) To promote and encourage highway construction, improvement, betterment, maintenance and marking for the guidance and warning of the users.

(2) To urge adoption of just and intelligent legislation on the use of highways and the regulation of traffic thereon.

(3) To maintain offices for collecting and disseminating information and the furnishing of advice and assistance to the owners of automobiles.

(4) To protect the legitimate interests of its members in connection with its purposes.

(5) To affiliate and associate with similar organizations.

The District Court also found (R. 83-84) that taxpayer, in furtherance of its purposes, "provided" during 1943 and 1944 the following:

(1) A Touring Bureau which provides the members with complete touring data and assists them in planning motor trips.

(2) An Emergency Road Service Department, which makes arrangements for the rendering of emergency road service to members who encounter

automobile trouble on the highways, which service is restricted to passenger cars.

(3) A Road Sign Department, which operates in conjunction with state and local authorities, a service consisting of the erection and maintenance of direction and warning signs and historical markers.

(4) A Public Safety Department, which carries on an active and aggressive campaign to reduce traffic accidents, eliminate traffic hazards and generally improve traffic conditions.

(5) An Adjustment and Traffic Department, which advises and assists the members with respect to traffic violations and accidents.

(6) A License Department, which assists members in the annual renewal of automobile registration with the State Department of Motor Vehicles and obtaining automobile license plates, as well as Federal auto tax stamps.

(7) A Magazine Department which publishes and distributes free to the members a magazine, keeping them informed of motoring conditions and improvements, and specializing in travel information with respect to trips to points of interest where members will find pleasure and recreation, and which has contained no paid advertising material since January 1, 1942.

The District Court concluded (R. 87) that the “association is and was at all times here pertinent a

club within the meaning of Section 101 (9) of the Internal Revenue Code" and that taxpayer (R. 89) "was organized and operated exclusively for pleasure, recreation and other nonprofitable purposes during the years 1943 and 1944".

Judgment was accordingly rendered in favor of taxpayer in the amount of \$232,865.12, with interest (R. 90-91), representing Federal income and excess profits taxes paid for the taxable years 1943 and 1944.

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#### **STATEMENT OF POINTS TO BE URGED.**

The principal point (R. 96-97) upon which the Government intends to rely is that the District Court erred in holding that taxpayer was, during the years 1943 and 1944, a club organized and operated exclusively for pleasure, recreation and other nonprofitable purposes within the meaning of the exempting statute.

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#### **SUMMARY OF ARGUMENT.**

Taxpayer was not a club within the meaning of Section 101 (9) of the Internal Revenue Code, since it had none of the attributes commonly associated with a club. That is, there was no provision made for social intercourse, its membership was unlimited, new members were not selected by ballot or otherwise chosen by members of the association, and there was no group activity or other club functions. It was merely an association organized and operated to render service to its

members in the operation of their automobiles and to promote and encourage highway construction and safe driving.

The taxpayer did not come within the statute for the further reason that it was not organized nor was it operated in 1943 or 1944 exclusively for the pleasure or recreation of its members. The undisputed facts clearly show that little, if any, of its activities were devoted to such purposes. The principal services rendered by taxpayer to its members consists primarily of insurance, road service and travel advice. Its other activities were of a semi-public nature having to do with highway construction and assisting state and local authorities in connection with traffic signs.

It is the Government's position that such activities were not sufficient to establish that taxpayer was organized and operated *exclusively* for the purposes specified in the exempting statute.

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#### ARGUMENT.

**TAXPAYER WAS NOT A "CLUB" UNDER THE ACT NOR WAS IT ORGANIZED AND OPERATED EXCLUSIVELY FOR PLEASURE OR RECREATION.**

Section 101 (9) of the Internal Revenue Code, *supra*, exempts from Federal income taxes certain types of "associations", including "Clubs organized and operated exclusively for pleasure, recreation, and other nonprofitable purposes". Taxpayer contends that it comes within the exemption. The Government takes the position that, on the undisputed facts, taxpayer

cannot bring itself within the exempting statute because (1) taxpayer is not a "club" within the meaning of the Act and (2) taxpayer was not "organized and operated *exclusively* for pleasure, recreation, and other [similar] nonprofitable purposes". (Italics supplied.)

That taxpayer is not a club for the purposes here concerned, seems clear. In the absence of a statutory definition or helpful legislative history it seems appropriate to conclude that Congress intended by the section to exempt organizations which are usually and commonly referred to as clubs. The word "club" is defined in Webster's New International Dictionary (Second ed., 1948), p. 509, as follows:

6. An association of persons for the promotion of some common object, as literature, science, politics, good-fellowship, etc., esp. one jointly supported and meeting periodically. Membership is usually conferred by ballot, and carries the privilege of exclusive use of club quarters.

A similar definition is found in Funk & Wagnalls' New Standard Dictionary (1947 ed.), p. 506, as follows:

An organization of persons who meet for social intercourse or other common object, the members of which are usually limited in number and chosen by ballot; \* \* \*

Taxpayer's members do not, as such, meet for social intercourse (R. 133) nor is its membership limited in number. (R. 136.) Moreover, membership is not conferred by ballot and members have no means of pass-

ing on the admission of new members. (R. 137.) In addition, taxpayer has no clubhouse or other meeting place. We find little, if anything, about taxpayer which makes it a club within the definitions of the word.

The Court below concluded that (R. 87) "A club is an association the expenses of which are shared among its members" and also concluded that (R. 87):

To constitute a club within the meaning of Section 101 (9) of the Internal Revenue Code it is not necessary that its activities include social features or a commingling of the members, one with another, in fellowship, but it is sufficient if its members make a common cause in a financial or other sense, or if there is present group activity.

We find no support for the conclusion that the mere sharing of expenses among individuals gives to the group the aspect of a club. Certainly that would not suffice as a definition of sufficient persuasion to import Congressional intent that no more would be needed to qualify under the statute. While it is true that the use of the word "club" does not necessarily carry with it the idea of social intercourse, it usually does so. It is incumbent upon taxpayer before it can enjoy the privileges of an exempting statute to show that it comes within the Act. It is not sufficient that taxpayer show that it is not necessarily excluded from the benefits, it must make a clear showing in the affirmative. It is common knowledge that when we refer to a club, we think of a clubhouse or some other place where the club members may meet socially. That is clear from the dictionary definitions.

It is difficult to understand what the lower Court had in mind by saying that "it is sufficient if its members make a common cause in a financial \* \* \* sense". (R. 87.) If the Court had in mind that a "club" within the meaning of the Act could be no more than a group of people interested in saving money on insurance and automobile service charges, we see no support whatever for the conclusion. It may be that the Court had in mind the exemption of business leagues, crop financing operations, domestic building and loan associations, fruit growers' associations, holding companies, teachers' retirement fund associations or the like. If so, they are covered by other subdivisions of Section 101 of the Internal Revenue Code and have no place in construing subsection (9), devoted exclusively to "clubs".

The entire record clearly shows that taxpayer has no activities commonly associated with club functions. Almost any motorist is familiar with so-called automobile clubs of which taxpayer is a typical example and it is common knowledge among motorists that such organizations are attractive solely because of the service they render the members in the operation of their automobiles and the insurance advantages afforded. It is sheer nonsense to suggest that anyone joins any so-called automobile club for any other reason than to receive the benefits offered in that direction. If he thinks about joining an association of this kind, his first and only consideration is whether or not the services and reduced insurance rates are worth the dues he will be required to pay. In no case

does he consider that he is joining the so-called "club" for pleasure or recreation.

It is significant also, in determining what Congress meant by "clubs", to note that Congress had in mind "pleasure" and "recreation". The indication is that the word "club" was used in the ordinary sense. Published administrative interpretation is to that effect. In G.C.M. 23688, 1943 Cum. Bull. 283, 286-287, the question is discussed as follows:

Although there is no statutory definition of the term "club," as used in section 101 (9) of the Code, it is believed that the term contemplates a commingling of members, one with the other, in fellowship. Thus, an organization should be so composed and its activities be such that fellowship among the members plays a material part in the life of the organization in order for it to come within the meaning of the term "club." \* \* \*

The term "clubs," as used in section 101 (9) of the Code, *supra*, is used in the same sense as the term "club" is used in section 1710 of the Code and corresponding sections of the Revenue Acts relating to the taxation of dues or membership fees paid to "any social, athletic, or sporting club or organization." (See G.C.M. 13067, *supra*.)

In *Arner v. Rogan* (May 20, 1940, unreported), the District Court of the United States for the Southern District of California, Central Division, had occasion to consider whether the Biltmore Health Club was a "club" within the meaning of section 501 of the Revenue Act of 1926, as amended by section 413 (a) of the Revenue Act of 1928 (now section 1710 of the Code). In conclud-

ing that the organization was not a club, the Court said:

\* \* \* at least there must be some sort of association or cooperation between the members in an effort to reach some common objective before we may consider that there is a club or organization.

In the course of its opinion, the Court observed:

The evidence shows that members never met together or in committee and never participated in any activities which are normally carried on by members of clubs or similar organizations, nor is there evidence that the patrons were entitled by the terms of their contracts to so participate. \* \* \*

Another factor given weight by the Court was that:

\* \* \* the Biltmore Health Club did not in practice restrict its membership, nor did it agree to do so. The only qualifications apparently were that the applicant be over 21, white, free from any contagious disease or dangerous physical condition, and able to pay the fees.

The necessary implication to be derived from the *Arner* case is that financial contribution by way of a fee charged by the organization does not amount to "association or cooperation between the members in an effort to reach some common objective," but that there must be some participation by the members in activities ordinarily carried on by clubs, which activities are intended to culminate in the realization of a common objective.

Although that ruling was issued in connection with a so-called automobile club differing in some respects from taxpayer, it will be seen that under the ruling taxpayer would not be exempt since it does not have the necessary attributes of a club and because it was not organized or operated exclusively for the purposes specified in the statute.

We think it is equally clear that taxpayer was not organized and operated exclusively for pleasure or recreation. The words of the statute "and other non-profitable purposes" do not, under the familiar rule of *ejusdem generis*, enlarge the meaning of the preceding words of the statute. Otherwise the word "exclusively" would be meaningless and the words "pleasure" and "recreation" would be mere surplusage.

There is no doubt that taxpayer does render an important public service in the promotion of good highways and safe driving. However, that fact is entirely immaterial in determining whether taxpayer is a club or whether it functions for the pleasure and recreation of its members. No doubt the members find considerable satisfaction and comfort in knowing that they will be towed to a garage (R. 130, 144) if necessity requires, or that an attorney of the association will come to their rescue in the event of arrest for a traffic violation. (R. 128.) The privilege of obtaining travel information and license plates without inconvenience (R. 160) as well as the privilege of obtaining inexpensive insurance (R. 140) is very pleasing to the members. However, that is not, we think, the pleasure

Congress had in mind in limiting the application of the exemption. Further, it cannot be seriously contended that rendering such services to its members puts the association in the category of operating "exclusively" for the promotion of pleasure and recreation. In interpreting a similar statute the Court in *Better Business Bureau v. United States*, 326 U.S. 279, held that the word "exclusive" in the statute meant just what it said and is not to be interpreted otherwise.

Taxpayer is in reality nothing more than a service organization. It renders services to its members for a consideration. The membership is large (R. 151), its net income is substantial (R. 131, Pltf. Ex. 1-H, 1-I), and its territory is extensive. (R. 149.) Anyone who has not demonstrated that he is a hazardous driver may join. (R. 136.) As above stated, there are no social aspects to the organization (R. 133) and there is nothing suggesting (except in an extremely remote way) that the recreation of its members is involved. The association will assist a member in planning a motor trip be it for a vacation or business. It does not devote all or even a substantial part of its income or of its attention to planning pleasure trips for its members.

The expression "pleasure car" might have had some factual significance when taxpayer was incorporated in 1907 but that was not so during the period here involved. Today a private car is virtually a necessity. Anyone knows that only a small fraction of the yearly

driving can be assigned to the pleasure or recreation of the driver. And so it is with the maintenance of that necessary and essential item in our daily lives. We need car service now more than ever before; however, very little of it nowadays can be assigned to pleasure or recreation expenses. Our car is needed to take us to the golf course or trout stream but pleasure and recreation starts after we get there. The golf club or rod and gun club may be income tax exempt under the section here involved, but the so-called automobile club that sends out the tow car or puts up the fine for traffic violations is a different type of organization. At least we believe most anyone, including members of Congress, would think so. To hold otherwise in applying Section 101 (9) of the Internal Revenue Code is, we submit, stretching the exempting statute to unreasonable limits. This is the first case involving an association of this kind and is quite obviously important from a revenue standpoint. We submit that the present administrative interpretation of the statute is correct and that the Commissioner of Internal Revenue was not in error in assessing and collecting the taxes here in question.

**CONCLUSION.**

The judgment in the lower Court should be reversed.

Dated, December 22, 1948.

Respectfully submitted,

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